
IN THE
Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-1871

GENERAL FOODS CORPORATION, *Petitioner,*

v.

UNITED STATES, *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF CLAIMS

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GENERAL FOODS CORPORATION, *Petitioner*,

v.

UNITED STATES, *Respondent*.

**PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF CLAIMS**

Petitioner, General Foods Corporation, prays that a writ of certiorari issue to review the opinion and judgment of the United States Court of Claims entered in these proceedings on January 28, 1976.

OPINION BELOW

The opinion and judgment of the Court of Claims, review of which is sought, is reported at 530 F.2d 923 and appears in the Appendix hereto. (App. 1a.)

JURISDICTION

The judgment of the Court of Claims was entered on January 23, 1976, and an application for a 60-day extension of time for filing a petition for writ of certio-

rari was filed by the petitioner, General Foods Corporation, on April 15, 1976. An order of this Court extending the time to file a petition for writ of certiorari to and including June 26, 1976, was issued on April 19, 1976. (App. 1a.) This petition for certiorari was timely filed within the period provided by the order extending the time to file a petition for writ of certiorari. This Court's jurisdiction is invoked under 28 U.S.C. § 1255(1).

QUESTIONS PRESENTED

I. Whether gain attributable to original issue discount received on the retirement of evidences of indebtedness issued after December 31, 1954, and before May 28, 1969, and held by the petitioner, General Foods Corporation, for periods of not more than six months is taxable as short-term capital gain pursuant to Section 1232 of the Internal Revenue Code of 1954.

II. Whether the Court of Claims erred in refusing jurisdiction over the petitioner's claim of unlawful discrimination.

STATUTES INVOLVED

This action arises under Section 1232 of the Internal Revenue Code of 1954, reproduced in this petition at pp. 5-6, *infra*.

STATEMENT OF THE CASE

During its taxable year 1959, beginning April 1, 1958, and ending March 31, 1959, petitioner General Foods Corporation ("General Foods") held promissory notes with no stated interest issued by various corporations. The notes, commonly referred to as commercial paper, were non-registered bearer instruments containing an unconditional promise to pay a specified

amount on a specified date at a specified place. General Foods purchased each of the notes from either the issuer or a dealer in securities for an amount less than the stated face value of the note. General Foods held the notes for less than six months, with the holding periods ranging from 43 days to 181 days. All of the notes involved were held to maturity and retired in the taxable year 1959, and at maturity General Foods received the face value of the notes from the issuers. The amount received by General Foods on retirement of each of the notes which exceeded the amount paid by General Foods for the note was original issue discount; no part of that amount received was attributable to market fluctuations as opposed to the passage of time.

General Foods Corporation is not now nor has it ever been a dealer in securities. The notes were purchased by General Foods for investment and did not constitute property of a type that would be held in inventory or for sale to customers in the normal course of business. All of the notes were issued after December 31, 1954, and before May 28, 1969. On its federal income tax return for the taxable year 1959 General Foods reported short-term capital gains of \$608,598.99, representing the difference between the purchase price of the notes and the face value of the notes received upon their retirement. For the taxable year 1959, General Foods had a net capital loss carry-over of \$518,840.74 which was used to partially offset the short-term capital gain received from the retirement of the notes.

In 1965, General Foods received a statement of tax due for the taxable year 1959 from the Commissioner of Internal Revenue ("Commissioner"). The deficiency assessment totalled \$345,638 plus interest, \$208,291 of which resulted from the Commissioner's treating as

interest income rather than as short-term capital gain the amounts received in excess of the purchase price on the retirement of the notes. General Foods paid the entire deficiency assessment including interest in 1965.

On November 6, 1967, General Foods filed a claim with the Commissioner seeking a refund in the amount of \$208,291 plus the interest paid thereon together with interest as provided by law. The refund claimed represented that portion of the assessed deficiency attributable to the Commissioner's treatment as ordinary interest income rather than as short-term capital gain the amounts received in excess of the purchase prices from retirement of the corporate notes. On March 1, 1971, the Commissioner disallowed General Foods' claim in its entirety, whereupon General Foods instituted suit in the Court of Claims. The Court of Claims, en banc, upheld the Commissioner's position and dismissed General Foods' petition and entered judgment against General Foods. Contrary to General Foods' position, the Court of Claims held that Section 1232 of the Internal Revenue Code of 1954 did not treat original issue discount received on notes held for six months or less as short-term capital gain, and that the original issue discount realized on the retirement of notes held by General Foods for six months or less was taxable as ordinary income.

REASONS FOR GRANTING THE WRIT

In deciding against General Foods, the Court of Claims ignored the meaning of the applicable statute and the stated Congressional intent. Put simply, the Court of Claims dismissed entirely the plainly-stated intent of Congress. This undermines the tax structure

established by Congress. This Court should redress this action.

Furthermore, the Court of Claims erred in refusing jurisdiction over General Foods' claim of unlawful discrimination, thereby denying General Foods a valid and independent ground for relief. This Court should clarify the jurisdiction of the Court of Claims.

I.

THE COURT OF CLAIMS DECISION DISREGARDS THE CONGRESSIONAL INTENT WITH RESPECT TO SECTION 1232 OF THE INTERNAL REVENUE CODE OF 1954

During the tax year here in question Section 1232 of the Internal Revenue Code of 1954 provided in relevant part as follows:

"SEC. 1232. BONDS AND OTHER EVIDENCES OF INDEBTEDNESS.

(a) GENERAL RULE.—For purposes of this subtitle, in the case of bonds, debentures, notes, or certificates or other evidences of indebtedness, which are capital assets in the hands of the taxpayer, and which are issued by any corporation, or government or political subdivision thereof—

(1) RETIREMENT.—Amounts received by the holder on retirement of such bonds or other evidences of indebtedness shall be considered as amounts received in exchange therefor

(2) SALE OR EXCHANGE.—

(A) GENERAL RULE.—Except as provided in subparagraph (B), upon sale or exchange of bonds or other evidences of indebtedness issued after December 31, 1954, held by the taxpayer more than 6 months, any gain real-

ized which does not exceed an amount which bears the same ratio to the original issue discount (as defined in subsection (b)) as the number of complete months that the bond or other evidences of indebtedness was held by the taxpayer bears to the number of complete months from the date of original issue to the date of maturity, shall be considered as gain from the sale or exchange of property, which is not a capital asset. Gain in excess of such amount shall be considered gain from the sale or exchange of a capital asset held more than 6 months.

* * *

(b) DEFINITIONS.—

(1) ORIGINAL ISSUE DISCOUNT.—For purposes of subsection (a), the term ‘original issue discount’ means the difference between the issue price and the stated redemption price at maturity. If the original issue discount is less than one-fourth of 1 percent of the redemption price at maturity multiplied by the number of complete years to maturity, then the issue discount shall be considered to be zero. For purposes of this paragraph, the term ‘stated redemption price at maturity’ means the amount fixed by the last modification of the purchase agreement and includes dividends payable at that time.”

* * *

When Congress enacted Section 1232 of the Internal Revenue Code of 1954, it established a statutory scheme for the treatment of gain realized from the retirement of original issue discount notes. Section 1232 of the Internal Revenue Code did not provide that the original issue discount realized from the retirement of a note held for six months or less should be treated as interest income. Instead, Section 1232(a)(1) estab-

lished the general rule that amounts received on the retirement of evidences of indebtedness which were capital assets in the hands of the taxpayer were to be treated as capital gain. Section 1232(a)(2)(A) provided an exception to the general rule stated in Section 1232(a)(1) by treating the original issue discount portion of the gain realized from the retirement of evidences of indebtedness held by a taxpayer for more than six months as gain from the sale or exchange of property which is not a capital asset. Since no exception was enacted to govern the original issue discount realized on the retirement of evidences of indebtedness held for six months or less, that gain was governed by the general rule of Section 1232(a)(1) and treated as capital gain.

The legislative history of Section 1232 makes plain the Congressional intent of that section. In enacting Section 1232 of the Internal Revenue Code of 1954, Congress was aware of the uncertainty regarding the treatment of original issue discount under the predecessor section to Section 1232:

“Under section 117(f) of present law, when a corporate or Government bond in registered form or with coupons attached is retired the transaction is treated as a sale or exchange. There is some uncertainty as to the status of proceeds in these transactions, i.e., as capital gain or as interest income where the bond or other evidence of indebtedness has been issued at a discount (see *I. T.* 3486, 1941-2, C.B. p. 76, as compared with *Comm. v. Caulkins*, 144 F.2d 482). In these cases, that part of the amount received on a sale or exchange which may represent a partial recovery of discount on original issue is a form of interest income and in fact is deductible as an interest payment by

the issuing corporation." S. Rep. No. 1622, 83d Cong., 2d Sess. 112 (1954); 3 U.S.C. Cong. & Adm. News 4745 (1954).

Congress resolved the question in enacting Section 1232:

"Paragraph (1) restates the content of present law. For bonds or other evidences of indebtedness issued after December 31, 1954, the bill abandons present restriction of capital treatment on retirement to bonds and other evidences of indebtedness which have interest coupons attached or which are in registered form. *Redemption of all bonds and other evidences of indebtedness will receive capital gain or loss treatment on redemption if issued after December 31, 1954, and if they are otherwise capital assets, except to the extent that the recovery of issue discount is subject to paragraph (2) [Section 1232(a)(2)].*" (emphasis added) H. Rep. No. 1337, 83d Cong., 2d Sess. A275 (1954); 3 U.S.C. Cong. & Adm. News 4417 (1954).

An identical statement is contained in the report of the Committee on Finance, S. Rep. No. 1622, 83d Cong., 2d Sess. 433; 3 U.S.C. Cong. & Adm. News 5076 (1954).

Section 1232 by its own words and by its legislative history plainly provided that on retirement of evidences of indebtedness held for six months or less, the gain realized, including the original issue discount, was to be treated as capital gain. As this Court stated in *Hanover Bank v. Commissioner*, 369 U.S. 672, 682 (1962), "[w]e are bound by the meaning of the words used by Congress, taken in light of the pertinent legislative history." And the Court of Claims failed to give proper effect to the specific provision, the specific

exception in Section 1232 that original issue discount on obligations held for *more* than six months "shall be considered as gain from the sale or exchange of property which is not a capital asset." This was the exception to the otherwise general rule of Section 1232. A statute must be read to give effect to all of its provisions, and not interpreted in a strained manner. *Jarecki v. G. D. Searle & Co.*, 367 U.S. 303, 307-308 (1961).

The Court of Claims relied upon *United States v. Midland-Ross Corp.*, 381 U.S. 54 (1965), and other case law for the proposition that original issue discount was ordinary income and not capital gain. *Midland-Ross*, however, was concerned with interpreting Section 117 of the 1939 Internal Revenue Code, prior to its amendment by Section 1232 of the 1954 Internal Revenue Code. This Court itself realized in *Midland-Ross* that Congress had enacted Section 1232 as part of the Internal Revenue Code of 1954 and stated that "we intimate no view on the construction of this statute." 381 U.S. at 59, n. 5. Additionally, this Court in *Commissioner v. National Alfalfa Dehydrating and Milling Co.*, 417 U.S. 134 (1974), noted that under the 1939 Internal Revenue Code it was unsettled whether income realized by an owner of an original issue discount obligation was taxable as ordinary income or as capital gain, and that this issue arising under the 1939 Internal Revenue Code was settled by *Midland-Ross*. But this Court also noted in *National Alfalfa* that "Congress, in enacting § 1232 of the 1954 Code, adopted a different approach to earned original issue discount. . . ." 417 U.S. at 146, n.9. That different approach is evidenced in the statutory language and legislative history of Section 1232.

Even the later restatement by Congress of its approach in 1954 was unheeded by the Court of Claims. In the Tax Reform Act of 1969, Pub. L. No. 91-172, 83 Stat. 487, Congress amended Section 1232 of the Internal Revenue Code of 1954 to alter the treatment of original issue discount. (App. 36a.) Under the change, a taxpayer is now required to include original issue discount realized on corporate obligations issued after May 27, 1969, in yearly income on a rateable basis over the life of the obligation, regardless of whether the notes are held for more than six months or for six months or less. Congress, in passing the Tax Reform Act of 1969, stated that the rules regarding original issue discount in effect until that time would continue to govern notes issued on or before May 27, 1969, and specifically stated that the rule in effect until 1969 for original issue discount on a bond held for six months or less was that original issue discount was treated as short-term capital gain:

"The rules provided by the bill regarding the treatment of original issue discount are not to apply in the case of bonds or other evidences of indebtedness issued by any government or political subdivision (or in the case of bonds or other evidence of indebtedness issued by a corporation on or before October 9, 1969). In these cases, the rules of present law regarding the treatment of original issue discount on the sale or exchange of a bond which is a capital asset in the hands of the taxpayer and which has been held by the taxpayer for more than 6 months are to continue to apply. In addition, in these cases, gain on the sale or exchange of a bond or other evidence of indebtedness which is a capital asset in the hands of the taxpayer but which has not been held by the taxpayer for more than 6 months is to be treated as a short-

term capital gain as under present law." (emphasis added) S. Rep. No. 552, 91st Cong., 1st Sess. 148 (1969); 2 U.S.C. Cong. & Adm. News 2180 (1969).

The Court of Claims, however, dismissed this statement of Congressional intent by holding that the views of a subsequent Congress as to the meaning of a statute enacted by a previous Congress do not carry great weight. This Court has said that "[s]ubsequent legislation declaring the intent of an earlier statute is entitled to great weight in statutory construction." *Red Lion Broadcasting Co. v. FCC*, 395 U.S. 367, 380-381 (1969). See *Mount Sinai Hospital of Greater Miami v. Weinberger*, 517 F.2d 329, 343 (5th Cir. 1975), *cert. denied*, 44 U.S.L.W. 3593 (Apr. 19, 1976).

The Court of Claims has interpreted the Internal Revenue Code explicitly rejecting the Congressional mandate. This Court should redress that imbalance.

II.

THE COURT OF CLAIMS ERRED IN REFUSING JURISDICTION OVER GENERAL FOODS' CLAIM OF UNLAWFUL DISCRIMINATION

The Commissioner's treatment of the original issue discount in this case as ordinary income rather than short-term capital gain unlawfully discriminates against General Foods. The answers filed by the Commissioner to interrogatories in *Boise Cascade Corporation v. United States*, 530 F.2d 1367 (Ct. Cl. 1976), (which answers were made a part of this case, App. 25a-28a.) establish that during the taxable period here in question the Commissioner did not tax as ordinary

income the income realized upon the retirement of original issue discount notes held for six months or less by similarly situated non-resident alien individuals and foreign corporations.

Pursuant to Sections 871(a)(1) and 881(a) of the Internal Revenue Code of 1954, a 30% tax rate was imposed on certain items of income received by non-resident alien individuals and foreign corporations from sources within the United States. (App. 29a, 33a.) The items of income which were subject to the tax included interest and other fixed or determinable periodical gains. In general, the tax imposed on these items was required to be withheld under Sections 1441 and 1442 of the 1954 Internal Revenue Code. (App. 33a, 35a.) During the taxable year in question, the Commissioner made no attempt to tax original issue discount on obligations held for six months or less as ordinary or interest income under Sections 871 and 881 or require withholding under Sections 1441 and 1442. Even after the Foreign Investors Tax Act of 1966, Pub. L. No. 89-809, 80 Stat. 1539, required that the income to be taxed to non-resident alien individuals and foreign corporations include amounts received on the retirement of evidences of indebtedness which are treated as gains from the sale of property which is not a capital asset, the Commissioner did not tax original issue discount received on obligations held for six months or less as ordinary or interest income. Apparently, the Commissioner believed that original issue discount received on obligations held for six months or less by a non-resident alien individual or foreign corporation was short-term capital gain. Otherwise the Commissioner would have taxed original issue discount received on obligations held for six months or less as ordinary or interest income under Sections 871 and 881.

There is no justification under the Internal Revenue Code for this discrimination between the domestic taxpayer in this case, General Foods, and foreign taxpayers. The courts have consistently held that discriminatory treatment of similarly situated taxpayers by the Internal Revenue Service is unlawful. As Mr. Justice Frankfurter stated in his concurring opinion in *United States v. Kaiser*, 363 U.S. 299, 308 (1960):

“The Commissioner cannot tax one and not tax another without some rational basis for the difference. And so, assuming the correctness of the principle of ‘equality,’ it can be an independent ground of decision that the Commissioner has been inconsistent, without much concern for whether we should hold as an original matter that the position the Commissioner now seeks to sustain is wrong.”

See *International Business Machines Corp. v. United States*, 343 F.2d 914 (Ct. Cl. 1965), *cert. denied*, 382 U.S. 1028 (1966).

Instead of determining whether unlawful discrimination existed, the Court of Claims held that since General Foods' claim for refund made no mention of unlawful discrimination, the Court of Claims was without jurisdiction to rule upon this issue.

The rule that a taxpayer cannot present one ground for relief in its claim and a different ground in its petition is designed to prevent surprise and to give adequate notice to the Commissioner of the nature of the claim and the facts, not to reward the Commissioner for concealing information which is solely within his possession. The rule cannot apply when the Commissioner has information exclusively within his own possession which would serve as a basis for a claim for refund and when the information is only subject to dis-

closure through judicial proceedings. General Foods' claim for refund stated that original issue discount received on the retirement of obligations held for six months or less should be treated as short-term capital gain under Section 1232. All of the relevant facts except for the Commissioner's own action in treating foreign taxpayers differently than General Foods were presented in the claim for refund. The case law on this issue has required that a taxpayer need only give "notice fairly advising the Commissioner of the nature of the taxpayer's claim." " *Kuehn v. United States*, 480 F.2d 1319, 1321 (Ct. Cl. 1973). Such notice was given by General Foods, but it was only in this very litigation by General Foods and by Boise Cascade suing for refunds after the claims for refund had been denied by the Commissioner that the Commissioner was forced to divulge his treatment of this very same kind of income in other taxpayers' hands.

The refusal of the Court of Claims to consider General Foods' claim of unlawful discrimination was an error by the Court of Claims regarding its own jurisdiction which this Court should correct.

CONCLUSION

For the above-stated reasons, the petition for writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX

1a

SUPREME COURT OF THE UNITED STATES

GENERAL FOODS CORPORATION, *Petitioner,*

v.

UNITED STATES

**Order Extending Time To File Petition for
Writ of Certiorari**

UPON CONSIDERATION of the application of counsel for petitioner(s),

IT IS ORDERED that the time for filing a petition for writ of certiorari in the above-entitled cause be, and the same is hereby, extended to and including June 26, 1976.

/s/ WARREN E. BURGER

Chief Justice of the United States.

Dated this 19th day of April, 1976.

IN THE UNITED STATES COURT OF CLAIMS

No. 70-73

(Decided January 28, 1976)

GENERAL FOODS CORPORATION v. THE UNITED STATES

David I. Granger, attorney of record, for plaintiff.
Harold D. Murry, Jr. and *Clifford, Warnke, Glass, McIlwain & Finney*, of counsel.

Richard F. Treacy, Jr., with whom was *Assistant Attorney General Scott P. Crampton*, for defendant. *Theodore D. Peyser* and *Donald H. Olson*, of counsel.

Before LARAMORE, *Senior Judge*, DAVIS, SKELTON, NICHOLS, KASHIWA, KUNZIG, and BENNETT, *Judges*.

Opinion

KASHIWA, *Judge*, delivered the opinion of the court:

This action comes before us on a stipulation of facts. The essential facts stipulated are recited below. Each of the parties claims that it is entitled to judgment on said stipulated facts. We hold for the defendant and against the plaintiff for reasons hereafter stated.

This is an action arising under the Internal Revenue Code of 1954 for the taxable year 1959, beginning April 1, 1958, and ending March 31, 1959. Since Section 1232 of the Internal Revenue Code of 1954 is the center of discussion, we shall first quote by footnote its relevant portions.¹

¹ SEC. 1232. BONDS AND OTHER EVIDENCES OF INDEBTEDNESS.

“(a) GENERAL RULE.—For the purposes of this subtitle, in the case of bonds, debentures, notes, or certificates or other evidences of indebtedness, which are capital assets in the hands of the taxpayer, and which are issued by any corporation, or government or political subdivision thereof—

“(1) RETIREMENT.—Amounts received by the holder on retirement of such bonds or other evidences of indebtedness shall be considered as amounts received in exchange therefor (except that in the case of bonds or other evidences of indebtedness issued before January 1, 1955, this paragraph shall apply only to those issued with interest coupons or in registered form, or to those in such form on March 1, 1954).

“(2) SALE OR EXCHANGE.—

“(A) GENERAL RULE.—Except as provided in subparagraph (B), upon sale or exchange of bonds or other evidences of indebtedness issued after December 31, 1954, held by the taxpayer more than 6 months, any gain realized which does not exceed—

“(i) an amount equal to the original issue discount (as defined in subsection (b)), or

“(ii) if at the time of original issue there was no intention to call the bond or other evidence of indebtedness before maturity, an amount which bears the same ratio to the original issue discount (as defined in subsection (b)) as the number of complete months

(Continued)

Plaintiff, General Foods Corporation, is a corporation duly organized and existing under the laws of the State of Delaware, with its principal place of business at White Plains, New York. The stipulation shows that General Foods Corporation's principal business is the production and sale of a wide variety of food and grocery products, many in package form under nationally advertised brand names. General Foods Corporation is not now, nor has it

(Continued)

that the bond or other evidence of indebtedness was held by the taxpayer bears to the number of complete months from the date of original issue to the date of maturity,

“shall be considered as gain from the sale or exchange of property which is not a capital asset. Gain in excess of such amount shall be considered gain from the sale or exchange of a capital asset held more than 6 months.

“(B) EXCEPTIONS.—This paragraph shall not apply to—

“(i) obligations the interest on which is not includible in gross income under section 103 (relating to certain governmental obligations), or

“(ii) any holder who has purchased the bond or other evidence of indebtedness at a premium.

“(C) DOUBLE INCLUSION IN INCOME NOT REQUIRED.—This section shall not require the inclusion of any amount previously includible in gross income.

“(b) DEFINITIONS.—

“(1) ORIGINAL ISSUE DISCOUNT.—For the purposes of subsection (a), the term “original issue discount” means the difference between the issue price and the stated redemption price at maturity. If the original issue discount is less than one-fourth of 1 percent of the redemption price at maturity multiplied by the number of complete years to maturity, then the issue discount shall be considered to be zero. For purposes of this paragraph, the term “stated redemption price at maturity” means the amount fixed by the last modification of the purchase agreement and includes dividends payable at that time.”

• • • • •

[As amended through 1959.]

ever been a dealer in securities. During the taxable year 1959, plaintiff held promissory notes with no stated interest issued by various corporations. The notes, commonly referred to as commercial paper, were non-registered bearer instruments containing an unconditional promise to pay a specified amount on a specified date at a specified place. Plaintiff purchased each of the notes from the issuer or from Goldman, Sachs & Company, a dealer in securities, at an amount less than its face value. The notes were held by plaintiff for periods ranging from 43 days to 181 days. The plaintiff held each note for a period less than six months and at maturity received the face amount from the issuer. Plaintiff retired all of the notes in the taxable year 1959. The notes were purchased by the plaintiff for investment and were not property of a type that would be held in inventory or for sale to customers in the normal course of business. All of the notes involved in this case were issued after December 31, 1954, and before May 27, 1969. The amount received by the plaintiff on retirement of each of the notes which exceeded the amount paid by plaintiff for the note was original issue discount; no part of that amount was attributable to market fluctuations as opposed to the passage of time.

On its Federal income tax return for the taxable year 1959, beginning April 1, 1958, and ending March 31, 1959, plaintiff reported short-term capital gains of \$608,598.99. This was the amount received over and above the purchase prices from the retirement at maturity of the total of \$90,750,000 non-interest-bearing corporate notes purchased by the plaintiff at a discount and held for less than six months. During the taxable year 1959 plaintiff had net capital loss carryovers from the prior years in the amount of \$518,840.74. There is no dispute as to this loss carryover. Plaintiff claims that it is entitled to deduct the loss carryover from the above-mentioned gain of \$608,598.99 because the gain is short-term capital gain.

On October 29, 1965, the Commissioner of Internal Revenue mailed to the plaintiff a statement of tax due, assessing a deficiency in income taxes for the taxable year 1959 in the amount of \$345,638 plus interest. Plaintiff paid this amount plus interest on November 8, 1965. The amount of \$208,291 of this deficiency assessment resulted from the Commissioner treating as interest income rather than as short-term capital gain the amount of \$608,598.99 received by plaintiff over and above the purchase prices on the retirement at maturity of the non-interest-bearing corporate notes purchased by the plaintiff at a discount for investment and held for less than six months. On November 6, 1967, plaintiff filed a claim for refund of this amount of \$208,291 plus the interest paid thereon together with interest as provided by law, representing that part of the assessed deficiency attributable to treating as interest income rather than short-term capital gain the amounts over and above the purchase prices, received by plaintiff on the retirement of the corporate notes. On March 1, 1971, the Commissioner of Internal Revenue disallowed in its entirety plaintiff's claim for refund. This action for refund was filed in this court on February 27, 1973.

Both parties agree that the sole issue presented is whether gain attributable to original issue discount on evidences of indebtedness issued after December 31, 1954, and before May 28, 1969, and held by plaintiff for periods of not more than six months is taxable as short-term capital gain on the retirement of the indebtedness.

The decision in this case rests, as we shall hereafter show, upon Section 1221 but since plaintiff's arguments center on Section 1232, we shall first examine Section 1232. Plaintiff claims that Section 1232 gives capital treatment to the gain in this case. Defendant, on the other hand, states that Section 1232 is not relevant to the original issue discount herein since Section 1232 only deals with notes which are capital assets in the hands of the taxpayer and since original issue

discount under case law is not a capital asset, Section 1232 does not apply.

We shall first discuss the history of Section 1232. Section 206(a)(1) of the Revenue Act of 1921, c. 136, 42 Stat. 227, 232, defined the term "capital gain" as "taxable gain from the sale or exchange of capital assets * * *." This provision, without material change, was reenacted by Section 208(a)(1) of the Revenue Act of 1924, c. 234, 43 Stat. 253, 262; by Section 208 (a)(1) of the Revenue Act of 1926, c. 27, 44 Stat. 9, 19; by Section 101(c)(1) of the Revenue Act of 1928, c. 852, 45 Stat. 791, 811; and by Section 101 (c)(1) of the Revenue Act of 1932, c. 209, 47 Stat. 169, 191.

The question arose as to whether, under these statutes, a redemption (retirement) of bonds constituted a sale or exchange within the meaning of that provision and successor statutes. A conflict of judicial decisions² on the matter led Congress to enact Section 117(f) of the Revenue Act of 1934, c. 277, 48 Stat. 680, 715, which is the predecessor of Section 1232(a)(1). The addition of that provision assured that the retirement of notes would constitute an exchange.

While Section 117(f) served to resolve the question of whether the *retirement* of a note constituted a "sale or exchange," it created a new round of litigation as to whether gain attributable to original issue discount was an amount received in exchange for a capital asset and, consequently, qualified for long-term capital gain treatment. In *Commissioner v. Caulkins*, 144 F.2d 482 (6th Cir. 1944), the Sixth Circuit read Section 117(f) to permit long-term capital gain treatment for the \$5,000 gain realized, functionally, as original issue discount. The court noted (at 484) that if the application of Section 117(f) resulted in inconsistencies and inequalities, "the correction of this defect in the operation of the statute is for Congress and not for the courts." The Supreme Court in *United States v. Midland-Ross Corp.*, 381

² See *Fairbanks v. United States*, 306 U.S. 436 (1939).

U.S. 54 (1965), subsequently disagreed with the holding of *Caulkins* that the proceeds received upon a face-amount certificate cannot be divided into separate increments which represent interest income and capital gain after other courts, including this court, refused to follow the rationale of the Sixth Circuit. See *Pattiz v. United States*, 160 Ct. Cl. 121, 311 F. 2d 947 (1963); *Commissioner v. Morgan*, 272 F. 2d 936 (9th Cir. 1959); *Rosen v. United States*, 288 F.2d 658 (3d Cir. 1961); *United States v. Harrison*, 304 F. 2d 835 (5th Cir. 1962), *cert. denied*, 372 U.S. 934 (1963).

The legislative history of the revised version of Section 117(f) (Section 1232) indicates that Congress chose to heed the admonition of the court in *Caulkins* to correct, at least partially, a possible defect in the statute which, under the holding of *Caulkins*, allowed the issuing corporation an interest deduction for original issue discount, but taxed the holder at more favorable long-term capital gain rates if the notes were held more than six months. The following language of the Senate Report accompanying the enactment of Section 1232 of the 1954 Code graphically illustrates the situation which Congress faced at the time (S. Rep. No. 1622, 83d Cong., 2d Sess. 112 (1954)):

(C) *Bonds and Other Debt (sec. 1232)*

(1) *House changes accepted by committee*

Under section 117(f) of present law, when a corporate or Government bond in registered form or with coupons attached is retired the transaction is treated as a sale or exchange. There is some uncertainty as to the status of proceeds in these transactions, i.e., as capital gain or as interest income where the bond or other evidence of indebtedness has been issued at a discount (see I.T. 3486, 1941-2, C.B. p. 76, as compared with *Comm. v. Caulkins*, 144 F. 2d 482). In these cases, that part of the amount received on a sale or exchange which may represent a partial recovery of discount on

original issue is a form of interest income and in fact is deductible as an interest payment by the issuing corporation.

Effective with respect to bonds issued after December 31, 1954, the House bill removes doubt in this area by providing that any gain realized by the holder of a bond attributable to the original issue discount will be taxed as ordinary income. * * *

The solution to the problem perceived by Congress as a result of *Caulkins* was a limited one. Together with other technical amendments to old Section 117(f), which amendments have no effect on the instant problem, Congress added subsection(a)(2) to Section 1232 to plug the revenue loss resulting from the allowance, under *Caulkins*, of long-term capital gain treatment.

Congress reenacted most of the text of Section 117(f) as Section 1232(a) of the 1954 Code and specifically added the limiting language "which are capital assets" to the language "bonds, debentures, notes, or certificates or other evidences of indebtedness." It explained this addition as follows (S. Rep. No. 1622, *supra*, at 434):

Section 117(f) does not itself extend capital-gain treatment to any transaction but simply provides one of several requirements for such treatment on retirement of certain securities. Paragraph (2) of this section [Section 1232], however, provides specifically for capital-gain treatment and, therefore, the phrase is inserted in the first sentence of this section to the effect that this section only applies to bonds and other evidences of indebtedness *which are capital assets* in the hands of the taxpayer. * * * [Emphasis supplied.]

We turn now from the history of the present positions of the parties. Plaintiff first argues that Section 1232 (a)(1) makes the retirement of these notes equal to an exchange.

Since the section does not provide for special treatment of original issue discount for notes held six months or less as it does for original issue discount on notes held more than six months in Section 1232 (a)(2), notes held for six months or less fall under Section 1232(a)(1). Their retirement is treated as an exchange and an exchange of a capital asset results in capital gain.

This is the point at which the parties separate. The defendant states that Section 1232(a)(1) does not apply; in fact, none of Section 1232 applies. In Section 1232(a) the general rule refers to notes "which are capital assets in the hands of the taxpayer." Defendant argues that under case law the original issue discount is separable from the note and is not a capital asset. Since Section 1232 is only applicable to capital assets, it does not apply to original issue discount on notes held for six months or less. Therefore, we must examine the case to determine how this item should be treated.

It has been held by the Supreme Court and other courts that an item of ordinary income derived from an income-producing capital asset retained its character even though sold as part of property which was a capital asset.³ In

³ *Watson v. Commissioner*, 345 U.S. 544 (1953) [profit from sale of an orange grove attributable to unmaturing crop was ordinary income]; *Commissioner v. Gillette Motor Transport, Inc.*, 364 U.S. 130 (1960) [award for wartime possession of trucking company by Government was rental income and not capital gain from involuntary conversion]; *Commissioner v. P. G. Lake, Inc.*, 356 U.S. 260 (1958) [consideration for assignment of oil payment right carved out from a larger mineral interest producing ordinary income was held to be taxable as ordinary income]; *Tunnell v. United States*, 259 F. 2d 916 (3d Cir. 1958) [proceeds of sale of interest in law partnership, to the extent attributable to accounts receivable, were taxable as ordinary income]; *Fisher v. Commissioner*, 209 F. 2d 513 (6th Cir. 1954) *cert. denied*, 347 U.S. 1014 [proceeds of sale of notes representing defaulted interest were ordinary income].

United States v. Midland-Ross Corp., *supra*, the Supreme Court held that original issue discount was ordinary income and not capital gain. The Court held as follows at 56-57:

* * * Although original issue discount becomes property when the obligation falls due or is liquidated prior to maturity and § 117(a)(1) defined a capital asset as "property held by the taxpayer," we have held that

"not everything which can be called property in the ordinary sense and which is outside the statutory exclusions qualifies as a capital asset. This Court has long held that the term 'capital asset' is to be construed narrowly in accordance with the purpose of Congress to afford capital-gains treatment only in situations typically involving the realization of appreciation in value accrued over a substantial period of time, and thus to ameliorate the hardship of taxation of the entire gain in one year." *Commissioner v. Gillette Motor Co.*, 364 U.S. 130, 134.

See also *Corn Products Co. v. Commissioner*, 350 U.S. 46, 52. In applying this principle, this Court has consistently construed "capital asset" to exclude property representing income items or accretions to the value of a capital asset themselves properly attributable to income. * * * [Footnote omitted.]

In an earlier decision in *Pattiz v. United States*, *supra*, this court held as follows:

We think the discount at which these notes were sold was in lieu of the payment of interest on them and that the difference in the amount paid for them and the amount at which they were redeemed was ordinary income. In our opinion it was not intended by § 117(f) of the Internal Revenue Code of 1939 to treat it as a capital gain. [160 Ct. Cl. at 128, 311 F. 2d at 950]

Judge Whitaker in his *Pattiz* opinion examines the relevant cases of several circuits and comes to the conclusion that

Section 117(f), the predecessor of Section 1232(a)(1), was intended to cover capital gain resulting from the retirement of a note in contrast to original issue discount gain representing compensation for the use of money.

That decision agrees with the Third Circuit's conclusion in *Rosen v. United States*, *supra*. In *Rosen* the taxpayer argued that Section 1232(a)(1) was an overriding statute which prevented original issue discount from being taxed as interest under Section 61. The court at 661 stated the issue to be:

* * * whether the requirement of Section 1232(a)(1) that amounts received on retirement of certain "evidences of indebtedness shall be considered as amounts received in exchange therefor" is tantamount to saying that the entire increment realized in such an exchange must be taxed as capital gain rather than ordinary income.

The court then looked at the tax treatment of fully earned increments upon the sale or exchange of capital assets and concluded that the general rule applies: the right to receive ordinary income from a capital asset is not changed into capital gain upon the sale of that asset together with the right. Section 1232(a)(1) did not abrogate that rule but, rather, provided for capital treatment for the capital increment which was realized upon retirement.

Plaintiff seizes upon a sentence in a Senate Committee on Finance Report to the Tax Reform Act of 1969, Pub. L. No. 91-172, 83 Stat. 487,⁴ to argue that Section 1232 was in-

⁴ S. Rep. No. 91-552, 91st Cong., 1st Sess. (1969) at 148:

"* * * In * * * [the case of Government evidences of indebtedness or in the case of pre-October 10, 1969, corporate evidences of indebtedness] gain on the sale or exchange of a bond or other evidence of indebtedness which is a capital asset in the hands of the taxpayer but which has not been held by the taxpayer for more than 6 months is to be treated as a short-term capital gain as under present law."

tended to overrule *Midland-Ross, supra*. This statement was made without any basis in the 1954 version of Section 1232. The views of a subsequent Congress as to the meaning of ambiguous language of a previous Congress do not carry great weight.⁵ An attempt to amend legislation of a previous Congress by Committee Report must be rejected.

Plaintiff also states that it should prevail because the Commissioner unlawfully discriminated in favor of similarly situated taxpayers. The basis of this claim is that the Commissioner failed to tax as ordinary income original issue discount on evidences of indebtedness held for six months or less by nonresident alien individuals and foreign corporations. In plaintiff's claim for refund no mention is made of a claim of unlawful discrimination. Accordingly, this court is without jurisdiction to rule upon a claim not set out in plaintiff's claim for refund. See Section 7422(a) of the 1954 Code and Treas. Reg. § 301.6402-2(b)(1) (1956); *Union Pacific R.R. v. United States*, 182 Ct. Cl. 103, 108, 389 F. 2d 437, 442 (1968), and the cases cited therein.

We find for the defendant and against the plaintiff. Plaintiff's petition is dismissed. Judgment is entered for the defendant and against the plaintiff.

⁵ *United States v. Price*, 361 U.S. 304, 313 (1960); *United States v. Philadelphia National Bank*, 374 U.S. 321, 348-49 (1963); *Waterman Steamship Corp. v. United States*, 381 U.S. 252, 269 (1965); *United States v. Southwestern Cable Co.*, 392 U.S. 157, 170 (1968); *Brown v. United States*, 192 Ct. Cl. 203, 210, 426 F. 2d 355, 357 (1970); and *Humble Oil & Refining Co. v. United States*, 194 Ct. Cl. 920, 932, 442 F. 2d 1362, 1369 (1971).

DAVIS, *Judge*, concurring in the result:

My vote to dismiss the petition is not founded on the use in section 1232 of "capital assets," the primary purpose of which I take to be to separate securities held for investment from those held in the ordinary course of trade or business. Rather, I am moved by the simple fact that section 1232 fails to deal at all with original issue discount on securities held for no more than six months, and therefore must conclude that the applicable rule, even under the 1954 code, was the "economic reality" of *United States v. Midland-Ross Corp.*, 381 U.S. 54 (1965), that such discount is equivalent to interest. Taxpayers can point to no part of section 1232 which lays down the treatment for original issue discount on bonds held for no more than six months. Subsection (a)(2)(A), as everyone agrees, is restricted on its face to evidences of indebtedness held for more than six months; subsection (a)(1) is no more than the equivalent of section 117(a)(4) of the 1939 Code which the Court in *Midland-Ross* held not a bar to treating original issue discount as ordinary income. The text of section 1232, in the initial 1954 Code, did not deal at all, as I read it, with the problem of original issue discount on bonds retained no more than half-a-year.

I agree with the taxpayer that the Congress which enacted that section may well have thought that original issue discount on such securities would thereafter be dealt with as short-term capital gain. But that was because that Congress mistakenly believed that *Commissioner v. Caulkins*, 144 F. 2d 482 (C.A. 6, 1944)—which had held all original issue discount on bonds held for investment to be capital gain—would continue as good tax law except insofar as the rule was changed in section 1232 for the longer-term securities. And the probability is that same Congress did not think it important to change the *Caulkins* rule for the no-more-than-six-months bonds because short-term capital gain is normally taxed at ordinary income rates. (The peculiar

situation now before us does not seem to have been in anyone's mind.)¹ At any rate, it seems to me clear that the Congress which enacted the 1954 Code did not adopt, in section 1232 or another provision, any rule for original issue discount on evidences of indebtedness held for no more than six months; it simply left that subject uncovered by specific rule. The result is that, since Congress has not imbedded any part of *Caulkins* in the Code, we are required to apply the rule of *Midland-Ross* which superseded and overruled *Caulkins*. Congress is not legislating when, instead of laying down a statutory rule, it leaves a subject alone, even though it may be content to let the matter be covered by a lower-court decision which later happens to be set aside by the Supreme Court. *Cf. Helvering v. Hallock*, 309 U.S. 106, 119-22 (1940).²

As for the claim of unlawful discrimination, I would rest squarely on the ground that the taxation of non-resident foreign taxpayers raises such different considerations that it cannot validly be compared, for equal protection purposes, to the taxation of domestic taxpayers.

¹ There is no solid indication that the section 1232 Congress affirmatively desired that original issue discount on bonds held for no more than six months should be treated as capital gain even if *Caulkins* should be overturned by the Supreme Court.

² The views of a later Congress on the earlier law have "very little, if any, significance." *United States v. Southwestern Cable Co.*, 392 U.S. 157, 170 (1968). Therefore weight should be given to the 1969 Senate report which said that "In . . . [the case of pre-1969 corporate indebtedness and Government bonds], gain on the sale or exchange of a bond or other evidence of indebtedness which is a capital asset in the hands of the taxpayer but which has not been held by the taxpayer for more than 6 months is to be treated as a short-term capital gain as under present law." S. REP. No. 91-552, 91st Cong., 1st Sess. 148 (1969) (1969-3 CUM. BULL. 518).

THE UNITED STATES COURT OF CLAIMS

GENERAL FOODS CORPORATION, *Plaintiff*,

v.

UNITED STATES OF AMERICA, *Defendant*

Stipulation of Facts

January 21, 1975

The following facts are stipulated between the parties for the purposes of this case only and subject to the right of either party to object to the relevance or materiality of any of the facts stated herein:

(1) The petition giving rise to this action was timely filed, and the Court has proper jurisdiction thereof under Section 1346(a)(1) and 1491 of Title 28 and Section 7422 (a) of Title 26 of the United States Code.

(2) This action arises under the Internal Revenue Code of 1954 and has been filed to seek a refund of Federal income taxes for the taxable year 1959, beginning April 1, 1958 and ending March 31, 1959. Plaintiff's petition is timely and Plaintiff is not barred from recovery of any refund of taxes claimed by statute of limitation defenses or by reason of the provisions of Section 6511 or 6532 of the Internal Revenue Code of 1954.

(3) Plaintiff in this action is General Foods Corporation. General Foods Corporation is a corporation duly organized and existing under the laws of the State of Delaware, with its principal place of business at 250 North Street, in the City of White Plains, County of Westchester, State of New York. General Foods Corporation's principal business is the production and sale of a wide variety of food and grocery products, many in package form under nationally advertised brand names. General Foods Corporation is not now, nor has it ever been, a dealer in securities.

(4) General Foods Corporation is the sole and absolute owner of claims herein presented, and no assignment or transfer of said claims nor any part thereof has been made.

(5) During the taxable year 1959, Plaintiff held promissory notes with no stated interest issued by various corporations. The notes (commonly referred to as commercial paper) were non-registered bearer instruments containing an unconditional promise to pay a specified amount on a specified date at a specified place. The notes were held by Plaintiff for terms ranging from 43 days to 181 days. Plaintiff purchased each of the notes from the issuer or from Goldman, Sachs & Co., a dealer in securities, at an amount less than its face value. The Plaintiff held each note for a period less than six months and at maturity received the face amount from the issuer. Plaintiff retired all of the notes in the taxable year 1959. The amount received by the Plaintiff on retirement of each of the notes which exceeded the amount paid by Plaintiff for the note was original issue discount; no part of that amount was attributable to market fluctuations as opposed to the passage of time.

(6) The notes were purchased by the Plaintiff for investment and were not property of a type that would be held in inventory or for sale to customers in the normal course of business.

(7) All of the notes involved in this case were issued after December 31, 1954 and before May 27, 1969. A summary of the transactions, by issuer, is set forth in Exhibit A attached hereto and incorporated herein.

(8) On December 15, 1959, Plaintiff duly and timely filed its Federal income tax return for the taxable year 1959 with the District Director, Internal Revenue Service, Manhattan District, New York; and at such place Plaintiff paid to such District Director by payments made December

15, 1958, March 16, 1959, June 15, 1959, and September 15, 1959, the sum of \$54,000,000 in connection therewith.

(9) Plaintiff reported on its income tax return for the taxable year beginning April 1, 1958 and ending March 31, 1959, short-term capital gains of \$608,598.99, the amount received, over and above the purchase price, from the retirement at maturity of the total of \$90,750,000 non-interest-bearing corporate notes purchased by the Plaintiff at a discount and held for less than six months.

(10) During the taxable year 1959 Plaintiff had net capital loss carryovers from prior years in the amount of \$518,840.74, which amount is available for deduction from the amounts received, over and above the purchase price, on the retirement of the notes in the event it is determined that those amounts are taxable as short-term capital gain.

(11) On October 29, 1965, the Commissioner of Internal Revenue mailed to the Plaintiff a Statement of Tax Due, assessing a deficiency in income taxes for the taxable year beginning April 1, 1958, and ending March 31, 1959, in the amount of \$345,638 plus interest, which sum plus interest was paid by Plaintiff to the aforementioned District Director on November 8, 1965.

(12) The amount of \$208,291 of this deficiency assessment resulted from the Commissioner treating as interest income rather than as short-term capital gain the amount of \$608,598.99 received by Plaintiff on the retirement at maturity of the non-interest-bearing corporate notes purchased by the Plaintiff at a discount for investment and held for less than six months.

(13) On November 6, 1967, Plaintiff duly and timely filed with the District Director a claim for refund of this amount of \$208,291 plus the interest paid thereon, together with interest as provided by law, representing that part of the previously assessed deficiency attributable to treating as interest income rather than short-term capital gain the

\$608,598.99 received by Plaintiff on the retirement of the notes described above in Paragraph 5. A copy of such claim for refund is attached hereto as Exhibit B and incorporated herein.

(14) On March 1, 1971, the Commissioner of Internal Revenue disallowed in its entirety Plaintiff's claim for refund. A copy of such notice disallowing Plaintiff's claim for refund is attached hereto as Exhibit C and incorporated herein.

(15) No part of the sum of \$208,291, the amount of tax claimed by Plaintiff, nor the deficiency interest paid by Plaintiff thereon, has been refunded to Plaintiff.

(16) Attached hereto as Exhibits D and E and incorporated herein are answers dated October 15, 1970 and March 8, 1971 to interrogatories, which answers were filed by the Commissioner of Internal Revenue in the presently pending case in this Court of *Boise Cascade Corporation and Subsidiary Companies v. United States*, Nos. 321-69 and 81-71.

/s/ DAVID I. GRANGER
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/s/ SCOTT P. CRAMPTON
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Assistant Attorney General
Tax Division

/s/ RICHARD F. TREACY, JR.
Attorneys for Defendant

January 16, 1975

Exhibit "A"
GENERAL FOODS CORPORATION
INFORMATION WITH RESPECT TO REDEMPTION OF CORPORATE NOTES
HELD BY GENERAL FOODS CORPORATION
TAXABLE YEAR BEGINNING APRIL 1, 1958 AND ENDING MARCH 31, 1959

Issuer	Purchase Date	Redemption Date	Holding Period	Purchase Price	Proceeds on Redemption
General Motors Acceptance Corporation	1/ 3/58	6/16/58	164 days	\$ 984,055.56	\$ 1,000,000.00
General Motors Acceptance Corporation	1/ 7/58	6/16/58	160 "	1,968,888.89	2,000,000.00
Yellow Manufacturing Acceptance Corporation	1/ 9/58	6/16/58	158 "	984,638.89	1,000,000.00
Yellow Manufacturing Acceptance Corporation	1/15/58	6/16/58	152 "	985,222.22	1,000,000.00
Yellow Manufacturing Acceptance Corporation	2/20/58	6/16/58	116 "	4,965,763.89	5,000,000.00
Yellow Manufacturing Acceptance Corporation	2/26/58	6/16/58	110 "	993,506.94	1,000,000.00
General Motors Acceptance Corporation	3/ 6/58	6/16/58	102 "	1,989,375.00	2,000,000.00
General Motors Acceptance Corporation	3/ 7/58	6/16/58	101 "	994,739.58	1,000,000.00
The Kroger Company	3/14/58	6/13/58	91 "	994,194.44	1,000,000.00
International Shoe Company	3/19/58	5/29/58	71 "	995,381.94	1,000,000.00
General Motors Acceptance Corporation	3/19/58	9/15/58	180 "	5,940,333.33	6,000,000.00
Yellow Manufacturing Acceptance Corporation	3/20/58	6/16/58	88 "	3,980,444.44	4,000,000.00
General Motors Acceptance Corporation	3/26/58	9/15/58	173 "	1,980,777.78	2,000,000.00
Yellow Manufacturing Acceptance Corporation	4/10/58	9/15/58	158 "	991,822.92	1,000,000.00
American Investment Company	6/ 4/58	9/15/58	103 "	995,750.00	1,000,000.00
American Investment Company	6/ 5/58	9/15/58	102 "	1,991,583.34	2,000,000.00
Yellow Manufacturing Acceptance Corporation	6/11/58	9/15/58	96 "	1,992,083.33	2,000,000.00
American Investment Company	6/12/58	9/15/58	95 "	1,992,166.66	2,000,000.00
J. P. Stevens & Company, Inc.	6/24/58	9/12/58	80 "	1,395,416.66	1,400,000.00
General Motors Acceptance Corporation	6/24/58	12/22/58	181 "	992,500.00	1,000,000.00
Yellow Manufacturing Acceptance Corporation	6/24/58	12/22/58	181 "	4,962,500.00	5,000,000.00
Commercial Factors Corporation	6/24/58	12/22/58	181 "	1,985,000.00	2,000,000.00
Meinhard-Commercial Corp.	6/24/58	12/22/58	181 "	992,500.00	1,000,000.00
William Iselin & Co., Inc.	6/24/58	12/22/58	181 "	1,985,000.00	2,000,000.00
Commercial Credit Corporation	7/ 2/58	9/15/58	75 "	997,395.83	1,000,000.00
California Packing Corporation	7/ 2/58	9/15/58	75 "	1,993,750.00	2,000,000.00
American Tobacco Company	7/ 2/58	9/30/58	90 "	1,992,500.00	2,000,000.00

Exhibit "A" (Continued)

GENERAL FOODS CORPORATION INFORMATION WITH RESPECT TO REDEMPTION OF CORPORATE NOTES HELD BY GENERAL FOODS CORPORATION TAXABLE YEAR BEGINNING APRIL 1, 1958 AND ENDING MARCH 31, 1959

Issuer	Purchase Date	Redemption Date	Holding Period	Purchase Price	Proceeds on Redemption
Yellow Manufacturing Acceptance Corporation	7/ 9/58	9/ 4/58	57 days	\$2,994,166.68	\$3,000,000.00
Commercial Credit Corporation	7/ 9/58	9/ 4/58	57 "	998,020.83	1,000,000.00
General Motors Acceptance Corporation	7/ 9/58	9/ 4/58	57 "	998,020.83	1,000,000.00
General Motors Acceptance Corporation	7/23/58	9/ 4/58	43 "	599,104.17	600,000.00
Yellow Manufacturing Acceptance Corporation	9/ 4/58	12/15/58	102 "	993,336.81	1,000,000.00
General Motors Acceptance Corporation	9/ 4/58	12/15/58	102 "	993,270.83	1,000,000.00
R. J. Reynolds Tobacco Company	9/ 9/58	12/15/58	97 "	1,985,486.11	2,000,000.00
Continental Can Company	9/11/58	12/ 4/58	84 "	993,659.12	1,000,000.00
California Packing Corporation	9/15/58	12/15/58	91 "	1,986,097.22	2,000,000.00
Yellow Manufacturing Acceptance Corporation	9/15/58	12/15/58	91 "	1,986,097.22	2,000,000.00
Yellow Manufacturing Acceptance Corporation	9/19/58	12/ 4/58	76 "	2,983,270.83	3,000,000.00
American Investment Company	10/ 6/58	12/ 4/58	59 "	2,985,864.57	3,000,000.00
R. J. Reynolds Tobacco Company	12/15/58	3/16/59	91 "	1,983,569.44	2,000,000.00
Yellow Manufacturing Acceptance Corporation	12/15/58	3/16/59	91 "	2,975,354.16	3,000,000.00
California Packing Corporation	12/18/58	3/16/59	88 "	1,984,111.12	2,000,000.00
American Tobacco Company	12/18/58	3/16/59	88 "	1,984,111.12	2,000,000.00
Yellow Manufacturing Acceptance Corporation	12/19/58	3/16/59	87 "	992,145.83	1,000,000.00
J. P. Stevens & Company, Inc.	12/22/58	3/ 4/58	72 "	993,500.00	1,000,000.00
Commercial Factors Corporation	12/22/58	3/ 4/58	72 "	1,988,000.00	2,000,000.00
William Iselin & Co., Inc.	12/22/58	3/ 4/58	72 "	1,988,000.00	2,000,000.00
Meinhard-Commercial Corp.	12/22/58	3/ 4/58	72 "	994,000.00	1,000,000.00
Sperry Rand Corporation	1/ 6/59	3/25/59	78 "	744,921.88	750,000.00
Totals				<u>\$90,141,401.01</u>	<u>\$90,750,000.00</u>

21a

Exhibit "B"

18

Int. Rev. Serv.
Manhattan, N. Y.

- ☒ Refund of Taxes Illegally, Erroneously or Excessively Collected.
- ☐ Refund of Amount Paid for Stamps Unused, or Used in Error or Excess.
- ☐ Abatement of Tax Assessed (not applicable to estate, gift, or income taxes).

Please Type or Print Plainly

Name of taxpayer or purchaser of stamps
General Foods Corporation (A Delaware Corporation)

Number and street
250 North Street

City, Town, State, Postal Zip Code
White Plains, New York 10602

Fill in applicable items—Attach letter size sheets
if space is not sufficient

- b. If an employer, enter employer identification number
13-0762680
- c. District in which return (if any) was filed
Manhattan District, New York
- d. Name and address shown on return, if different from above
General Foods Corporation
250 Park Avenue, New York 17, N. Y. and
250 North Street, White Plains, N. Y. 10602
- e. Period—if for tax reported on annual basis, prepare separate form for each taxable year
From April 1, 1958 to March 31, 1959
- f. Kind of tax
Income

Exhibit "B" (Continued)

g. Amount of assessment
\$53,769,046.40

Dates of payment

December 15, 1958, March 16, 1959, June 15, 1959,
September 15, 1959, November 8, 1965

i. Amount to be refunded (if income tax, complete computation below)
\$208,291.

k. The claimant believes that this claim should be allowed for the following reasons:

See Rider Attached

Computation of Income Tax Refund	Income Tax
1. Tax withheld	—0—
2. Estimated tax paid	19,564,000
3. Tax paid with original return	34,436,000
4. Any additional income tax paid	345,638
5. Total tax paid (Add lines 1-4)	54,345,638
6. Less : Your computation of correct tax	53,560,755
7. Amount of overpayment	784,883
8. Amount previously refunded	576,592
9. Net overpayment (Enter in item 1 above) ...	208,291

Under penalties of perjury, I declare that this claim, including any accompanying schedules and statements, has been examined by me and to the best of my knowledge and belief it is true and correct.

Dated October 31, 1967 Signed
Treasurer

Exhibit "B" (Continued)

GENERAL FOODS CORPORATION
(A Delaware Corporation)

RIDER ATTACHED TO CLAIM FOR REFUND OF FEDERAL INCOME
TAXES FOR THE TAXABLE YEAR APRIL 1, 1958 TO MARCH
31, 1959

Claimant, not a dealer in securities, reported in its income tax return for the fiscal year beginning April 1, 1958 and ended March 31, 1959 short-term capital gain of \$608,598.99, resulting from the redemption at maturity of non-interest-bearing corporation notes originally issued at a discount and purchased by the claimant, and held for six months or less.

Upon review of the claimant's income tax return for its taxable year beginning April 1, 1958 and ended March 31, 1958, claimant was assessed a tax deficiency of \$345,638 plus interest. Part of this deficiency was the result of treating the above-described \$608,598.99 as interest income rather than as short-term capital gain.

Claimant contends that Section 1232(a)(2) of the Internal Revenue Code of 1954 applies only to discounted notes held for *more* than six months and that since there is no specific provision within Section 1232(a)(2) for discounted notes held for six months or less, gain from redemption of such notes should be accorded short-term capital gain treatment.

Claimant therefore respectfully requests a refund of \$208,291, or such greater amount as may be legally refunded, together with interest thereon, representing that part of the previously assessed deficiency attributable to treating as interest income the \$608,598.99 gain from redemption at maturity of non-interest bearing corporation notes originally issued at a discount and held for six months or less.

24a

Exhibit "C"

SERVICE CENTER

NORTH-ATLANTIC REGION

Date: March 1, 1971 In reply refer to:

General Foods Corporation
(A Delaware Corporation)

250 North St.

White Plains, NY 10602

Social Security Number or Employer Identification
Number: 13-0762680

Document Locator Number: CR000

Type of Tax: 1120-Corporation Income Return

Period Ending: March 1959

Amount Claimed: \$208,291.00

Date Claim Received: November 6, 1967

Dear Taxpayer:

We have examined your claim for an adjustment of your taxes. I am sorry to tell you that we cannot allow your claim for the reasons stated below. This decision rests on certain provisions of the internal revenue laws and regulations.

This letter is your legal notice that your claim is disallowed in full.

If you wish to begin suit or proceedings for the recovery of any taxes, penalties, or other moneys for which this notice of disallowance is issued, the law requires you to do so within 2 years from the mailing date of this letter.

Sincerely yours,

/s/ F. L. BOSWITT
Director

Reasons for disallowance:

Full disallowance of claim per Appellate determination.

25a

Exhibit "D"

IN THE UNITED STATES COURT OF CLAIMS

No. 321-69

BOISE CASCADE CORPORATION and SUBSIDIARY COMPANIES,
Plaintiffs

v.

UNITED STATES OF AMERICA, *Defendant*

Response to Plaintiffs' Interrogatories

Oct. 15, 1970

Donald W. Bacon, being duly sworn, responds to plaintiffs' interrogatories as follows:

1. I hold the position of Assistant Commissioner, Compliance, Internal Revenue Service.

2. Plaintiffs' Interrogatory 1 reads as follows:

State whether the Commissioner of Internal Revenue requires payment of United States income taxes under sections 871(a)(1) and 881(a) of the Internal Revenue Code of 1954 with respect to original issue discount on bonds or other evidences of indebtedness issued after December 31, 1954, where such bonds or other evidences of indebtedness are held by a nonresident alien individual or foreign corporation for a period of not more than six months and such original issue discount is from United States sources but is not effectively connected with the conduct of a trade or business within the United States.

3. Plaintiffs' interrogatory 3 reads as follows:

State whether the Commissioner of Internal Revenue requires withholding of United States income taxes under section 1441 and 1442 of the Internal Revenue Code of 1954 with respect to original issue discount on bonds or other evidences of indebtedness issued after December 31, 1954, where such bonds or other evidences of indebtedness are held by a non-resident alien individual or foreign corporation for a period of not more than six months and such original issue discount is from United States sources but is not effectively connected with the conduct of a trade or business within the United States.

4. My answer to these two interrogatories is as follows:

To the best of my knowledge and belief the Commissioner did not require during the years in suit, 1955 through 1958, the payment of United States income taxes under sections 871(a)(1) and 881(a) of the Internal Revenue Code of 1954, or the withholding of United States income taxes under sections 1441 and 1442 of the Internal Revenue Code of 1954, with respect to original issue discount on bankers' acceptances and commercial paper, where such instruments were sold or redeemed by nonresident alien individuals or corporations, nor was the payment of tax or withholding required with respect to the discount element of United States Treasury bills when they were sold by such persons. However, upon the redemption of Treasury bills by nonresident aliens both the payment of tax and withholding was required.

/s/ DONALD W. BACON
Donald W. Bacon

Exhibit "E"

IN THE UNITED STATES COURT OF CLAIMS

No. 321-69

BOISE CASCADE CORPORATION and SUBSIDIARY COMPANIES,
Plaintiffs

v.

UNITED STATES OF AMERICA, *Defendant*

Response to Plaintiffs' Interrogatories

(Filed March 8, 1971)

Donald W. Bacon, being duly sworn, responds to plaintiffs' interrogatories as follows:

1. I hold the position of Assistant Commissioner, Compliance, Internal Revenue Service.

2. Plaintiffs' interrogatory 1 reads as follows:

State whether the Commissioner of Internal Revenue requires payment of United States income taxes under sections 871(a)(1) and 881(a) of the Internal Revenue Code of 1954 with respect to original issue discount on bonds or other evidences of indebtedness issued after December 31, 1954, where such bonds or other evidences of indebtedness are held by a non-resident alien individual or foreign corporation for a period of not more than six months and such original issue discount is from United States sources but is not effectively connected with the conduct of a trade or business within the United States.

3. Plaintiffs' interrogatory 3 reads as follows:

State whether the Commissioner of Internal Revenue requires withholding of United States income taxes under section 1441 and 1442 of the Internal Revenue Code of 1954 with respect to original issue discount on bonds or other evidences of indebtedness issued after December 31, 1954, where such bonds or other evidences of indebtedness are held by a nonresident alien individual or foreign corporation for a period of not more than six months and such original issue discount is from United States sources but is not effectively connected with the conduct of a trade or business within the United States.

4. My answer to these two interrogatories is as follows:

To the best of my knowledge and belief the Commissioner does not presently require the payment of United States income taxes under sections 871(a)(1) and 881(a) of the Internal Revenue Code of 1954, or the withholding of United States income taxes under sections 1441 and 1442 of the Internal Revenue Code of 1954, with respect to original issue discount on bankers' acceptances and commercial paper issued prior to May 28, 1969, where such instruments are sold or redeemed by nonresident alien individuals or corporations, nor is the payment of tax or withholding required with respect to the discount element of United States Treasury bills which are sold by such persons. However, upon the redemption of Treasury bills by nonresident aliens both the payment of tax and withholding is required.

/s/ DONALD W. BACON
Donald W. Bacon

INTERNAL REVENUE CODE OF 1954

§ 871. Tax on nonresident alien individuals

(a) No United States business and gross income of not more than \$15,400.

(1) **Imposition of tax.**—Except as otherwise provided in subsection (b) there is hereby imposed for each taxable year, in lieu of the tax imposed by section 1, on the amount received, by every nonresident alien individual not engaged in trade or business within the United States, from sources within the United States, as interest (except interest on deposits with persons carrying on the banking business), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income (including amounts described in section 402(a)(2), section 631(b) and (c), and section 1235, which are considered to be gains from

¹² In the view I take of the case, this conclusion renders moot two subsidiary points raised by the parties. First, plaintiff argues that defendant's treatment of original issue discount in the present case is so different from the treatment accorded such discount in the hands of nonresident aliens and foreign corporations as to be illegally discriminatory in favor of foreign persons and against United States persons. However, should my view of the law prevail, there is no such discrimination, and the question becomes moot. Secondly, while conceding that gain attributable to original issue discount on evidences of indebtedness *held for more than 6 months* is taxed only in the year realized through sale or exchange (Df's Brief, p. 24), defendant contends that on short-term evidences of indebtedness held by accrual basis taxpayers (such as plaintiffs), the original issue discount is taxable on a ratably accrued basis in the same manner as ordinary interest income. However, my treatment of such discount as short-term capital gain places the question within the general scope of defendant's concession that discount on longer term evidences of indebtedness is taxable only when realized, thus eliminating the question.

the sale or exchange of capital assets), a tax of 30 percent of such amount.

(2) Capital gains of aliens temporarily present in the United States.—In the case of a nonresident alien individual not engaged in trade or business in the United States, there is hereby imposed for each taxable year, in addition to the tax imposed by paragraph (1)—

(A) if he is present in the United States for a period or periods aggregating less than 90 days during such taxable year—a tax of 30 percent of the amount by which his gains, derived from sources within the United States, from sales or exchanges of capital assets effected during his presence in the United States exceed his losses, allocable to sources within the United States, from such sales or exchanges effected during such presence; or

(B) if he is present in the United States for a period or periods aggregating 90 days or more during such taxable year—a tax of 30 percent of the amount by which his gains, derived from sources within the United States, from sales or exchanges of capital assets effected at any time during such year exceed his losses, allocable to sources within the United States, from sales or exchanges effected at any time during such year.

For purposes of this paragraph gains and losses shall be taken into account only if, and to the extent that, they would be recognized and taken into account if such individual were engaged in trade or business in the United States, except that such gains and losses shall be computed without regard to section 1202 (relating to deduction for capital gains) and such

losses shall be determined without the benefits of the capital loss carryover provided in section 1212.

(b) No United States business and gross income of more than \$15,400.—A nonresident alien individual not engaged in trade or business within the United States shall be taxable without regard to subsection (a) if during the taxable year the sum of the aggregate amount received from the sources specified in subsection (a)(1), plus the amount by which gains from sales or exchanges of capital assets exceed losses from such sales or exchange (determined in accordance with subsection (a)(2)) is more than \$15,400, except that—

(1) the gross income shall include only income from the sources specified in subsection (a)(1) plus any gain (to the extent provided in subchapter P; sec. 1201 and following, relating to capital gains and losses) from a sale or exchange of a capital asset if such gain would be taken into account were the tax being determined under subsection (a)(2);

(2) the deductions (other than the deduction for charitable contributions and gifts provided in section 873(c)) shall be allowed only if and to the extent that they are properly allocable to the gross income from the sources specified in subsection (a), except that any loss from the sale or exchange of a capital asset shall be allowed (to the extent provided in subchapter P without the benefit of the capital loss carryover provided in section 1212) if such loss would be taken into account were the tax being determined under subsection (a)(2);

(3) the taxes imposed by this subtitle (under section 1, or under section 1201(b)) shall, in no case, be less than 30 percent of the sum of—

(A) the aggregate amount received from the sources specified in subsection (a)(1), plus

(B) the amount, determined under subsection (a)(2), by which gains from sales or exchanges of capital assets exceed losses from such sales or exchanges.

(c) United States business.—A nonresident alien individual engaged in trade or business within the United States shall be taxable without regard to subsection (a). For purposes of part I, this section, sections 881 and 882, and chapter 3, the term “engaged in trade or business within the United States” includes the performance of personal services within the United States at any time within the taxable year, but does not include the performance of personal services—

(1) for a nonresident alien individual, foreign partnership, or foreign corporation, not engaged in trade or business within the United States, or

(2) for an office or place of business maintained by a domestic corporation in a foreign country or in a possession of the United States,

by a nonresident alien individual temporarily present in the United States for a period or periods not exceeding a total of 90 days during the taxable year and whose compensation for such services does not exceed in the aggregate \$3,000. Such term does not include the effecting, through a resident broker, commission agent, or custodian, of transactions in the United States in stocks or securities, or in commodities (if of a kind customarily dealt in or an organized commodity exchange, if the transaction is of the kind customarily consummated at such place, and if the alien, partnership, or corporation has no office or place of business in the United States at any time during the taxable year through which or by the direction of which such transactions in commodities are effected).

(d) Doubling of tax.—

For doubling of tax on citizens of certain foreign countries, see section 891.

§ 881. Tax on foreign corporations not engaged in business in United States.

(a) Imposition of tax.—In the case of every foreign corporation not engaged in trade or business within the United States, there is hereby imposed for each taxable year, in lieu of the taxes imposed by section 11, a tax of 30 percent of the amount received from sources within the United States as interest (except interest on deposits with persons carrying on the banking business), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income (including amounts described in section 631(b) and (c) which are considered to be gains from the sale or exchange of capital assets).

(b) Doubling of tax.—

For doubling of tax on corporations of certain foreign countries, see section 891.

§ 1441. Withholding of tax on nonresident aliens

(a) General rule.—Except as otherwise provided in subsection (c), all persons, in whatever capacity acting (including lessees or mortgagors of real or personal property, fiduciaries, employers, and all officers and employees of the United States) having the control, receipt, custody, disposal, or payment of any of the items of income specified in subsection (b) (to the extent that any of such items constitutes gross income from sources within the United States), of any nonresident alien individual, or of any partnership not engaged in trade or business within the

United States and composed in whole or in part of non-resident aliens, shall (except in the cases provided for in section 1451 and except as otherwise provided in regulations prescribed by the Secretary or his delegate under section 874) deduct and withhold from such items a tax equal to 30 percent thereof.

(b) Income items.—The items of income referred to in subsection (a) are interest (except interest on deposits with persons carrying on the banking business paid to persons not engaged in business in the United States), dividends, rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income, and amounts described in section 402(a)(2), section 631(b) and (c), and section 1235, which are considered to be gains from the sale or exchange of capital assets.

(c) Exceptions.—

(1) Dividends of foreign corporations.—No deduction or withholding under subsection (a) shall be required in the case of dividends paid by a foreign corporation unless (A) such corporation is engaged in trade or business within the United States, and (B) more than 85 percent of the gross income of such corporation for the 3-year period ending with the close of its taxable year preceding the declaration of such dividends (or for such part of such period as the corporation has been in existence) was derived from sources within the United States as determined under part I of subchapter N of chapter 1.

(2) Owner unknown.—The Secretary or his delegate may authorize the tax under subsection (a) to be deducted and withheld from the interest upon any securities the owners of which are not known to the withholding agent.

(3) Bonds with extended maturity dates.—The deduction and withholding in the case of interest on bonds, mortgages, or deeds of trust or other similar obligations

of a corporation, within subsections (a), (b), and (e) of section 1451 were it not for the fact that the maturity date of such obligations has been extended on or after January 1, 1934, and the liability assumed by the debtor exceeds 27½ percent of the interest, shall not exceed the rate of 27½ percent per annum.

(4) Compensation of certain aliens.—Under regulations prescribed by the Secretary or his delegate, there may be exempted from deduction and withholding under subsection (a) the compensation for personal services of nonresident alien individuals who enter and leave the United States at frequent intervals.

(5) Special items.—In the case of amounts described in section 402(a)(2), section 631(b) and (c), and section 1235, which are considered to be gains from the sale or exchange of capital assets, the amount required to be deducted and withheld shall, if the amount of such gain is not known to the withholding agent, be such amount, not exceeding 30 percent of the proceeds from such sale or exchange, as may be necessary to assure that the tax deducted and withheld shall not be less than 30 percent of such gain.

(d) Alien resident of Puerto Rico.—For purposes of this section, the term “nonresident alien individual” includes an alien resident of Puerto Rico.

§ 1442. Withholding of tax on foreign corporations

In the case of foreign corporations subject to taxation under this subtitle not engaged in trade or business within the United States, there shall be deducted and withheld at the source in the same manner and on the same items of income as is provided in section 1441 or section 1451 a tax equal to 30 percent thereof; except that, in the case of interest described in section 1451 (relating to tax-free cove-

nant bonds), the deduction and withholding shall be at the rate specified therein.

Section 1232, as amended by the Tax Reform Act of 1969, Pub.L.No. 91-172, 83 Stat. 487:

Sec. 1232. Bonds and Other Evidences of Indebtedness.

(a) General Rule.—For purposes of this subtitle, in the case of bonds, debentures, notes or certificates or other evidences of indebtedness, which are capital assets in the hands of the taxpayer, and which are issued by any corporation, or by any government or political subdivision thereof—

(1) Retirement.—Amounts received by the holder on retirement of such bonds or other evidences of indebtedness shall be considered as amounts received in exchange therefor (except that in the case of bonds or other evidences of indebtedness issued before January 1, 1955, this paragraph shall apply only to those issued with interest coupons or in registered form, or to those in such form on March 1, 1954).

(2) Sale or Exchange.—

(A) Corporate Bonds Issued After May 27, 1969.—Except as provided in subparagraph (C), on the sale or exchange of bonds or other evidences of indebtedness issued by a corporation after May 27, 1969, held by the taxpayer more than 6 months, any gain realized shall (except as provided in the following sentence) be considered gain from the sale or exchange of a capital asset held for more than 6 months. If at the time of original issue there was an intention to call the bond or other evidence of indebtedness before maturity, any gain realized on the sale or exchange thereof which does not exceed an amount equal to the original issue discount (as defined in subsection (b)) reduced by the portion of original is-

sue discount previously includible in the gross income of any holder (as provided in paragraph (3)

(B)) shall be considered as gain from the sale or exchange of property which is not a capital asset.

(B) Corporate bonds issued on or before May 27, 1969, and government bonds.—Except as provided in subparagraph (C), on the sale or exchange of bonds or other evidences of indebtedness issued by a government or political subdivision thereof after December 31, 1954, or by a corporation after December 31, 1954, and on or before May 27, 1969, held by the taxpayer more than 6 months, any gain realized which does not exceed—

(i) an amount equal to the original issue discount (as defined in subsection (b)), or

(ii) if at the time of original issue there was no intention to call the bond or other evidence of indebtedness before maturity, an amount which bears the same ratio to the original issue discount (as defined in subsection (b)) as the number of complete months that the bond or other evidence of indebtedness was held by the taxpayer bears to the number of complete months from the date of original issue to the date of maturity,

shall be considered as gain from the sale or exchange of property which is not a capital asset. Gain in excess of such amount shall be considered gain from the sale or exchange of a capital asset held more than 6 months.

(C) Exceptions.—This paragraph shall not apply to—

(i) obligations the interest on which is not includible in gross income under section 103 (relating to certain governmental obligations), or

(ii) any holder who has purchased the bond or other evidence of indebtedness at a premium.

(D) Double inclusion in income not required.—

This section shall not require the inclusion of any amount previously includible in gross income.

(3) Inclusion in income of original issue discount on corporate bonds issued after May 27, 1969.—

(A) General rule.—There shall be included in the gross income of the holder of any bond or other evidence of indebtedness issued by a corporation after May 27, 1969, the ratable monthly portion of original issue discount multiplied by the number of complete months (plus any fractional part of a month determined in accordance with the last sentence of this subparagraph) such holder held such bond or other evidence of indebtedness during the taxable year. Except as provided in subparagraph (B), the ratable monthly portion of original issue discount shall equal the original issue discount (as defined in subsection (b)) divided by the number of complete months from the date of original issue to the stated maturity date of such bond or other evidence of indebtedness. For purposes of this section, a complete month commences with the date of original issue and the corresponding day of each succeeding calendar month (or the last day of a calendar month in which there is no corresponding day); and, in any case where a bond or other evidence of indebtedness is acquired on any other day, the ratable monthly portion of original issue discount for the complete month in which such acquisition occurs shall be allocated between the transferor and the transferee in accordance with the number of days in such complete month each held the bond or other evidence of indebtedness.

(B) Reduction in case of any subsequent holder.—

For purposes of this paragraph, the ratable monthly portion of original issue discount shall not include an amount, determined at the time of any purchase after the original issue of such bond or other evidence of indebtedness, equal to the excess of—

(i) the cost of such bond or other evidence of indebtedness incurred by such holder, over

(ii) the issue price of such bond or other evidence of indebtedness increased by the portion of original discount previously includible in the gross income of any holder (computed without regard to this subparagraph).

divided by the number of complete months (plus any fractional part of a month commencing with the date of purchase) from the date of such purchase to the stated maturity date of such bond or other evidence of indebtedness.

(C) Purchase defined.—For purposes of subparagraph (B), the term “purchase” means any acquisition of a bond or other evidence of indebtedness, but only if the basis of the bond or other evidence of indebtedness is not determined in whole or in part by reference to the adjusted basis of such bond or other evidence of indebtedness in the hands of the person from whom acquired, or under section 1014 (a) (relating to property acquired from a decedent).

(D) Exceptions.—This paragraph shall not apply to any holder—

(i) who has purchased the bond or other evidence of indebtedness at a premium, or

(ii) which is a life insurance company to which section 818(b) applies.

(E) Basis adjustments.—The basis of any bond or other evidence of indebtedness in the hands of the holder thereof shall be increased by the amount included in his gross income pursuant to subparagraph (A).

(b) Definitions.—

(1) Original issue discount.—For purposes of subsection (a), the term “original issue discount” means the difference between the issue price and the stated redemption price at maturity. If the original issue discount is less than one-fourth of 1 percent of the redemption price at maturity multiplied by the number of complete years to maturity, then the issue discount shall be considered to be zero. For purposes of this paragraph, the term “stated redemption price at maturity” means the amount fixed by the last modification of the purchase agreement and includes dividends payable at that time.

(2) Issue price.—In the case of issues of bonds or other evidences of indebtedness registered with the Securities and Exchange Commission, the term “issue price” means the initial offering price to the public (excluding bond houses and brokers) at which price a substantial amount of such bonds or other evidences of indebtedness were sold. In the case of privately placed issues of bonds or other evidence of indebtedness, the issue price of each such bond or other evidence of indebtedness is the price paid by the first buyer of such bond increased by the amount, if any, of tax paid under section 4911 (and not credited, refunded, or reimbursed) on the acquisition of such bond or evidence of indebtedness by the first buyer. For purposes of this paragraph, the terms “initial offering price” and “price paid by the first buyer” include the aggregate payments made by the purchaser under the purchase agreement, including modifications thereof. In the case of a bond or other evidence of indebtedness and an option or other se-

curity issued together as an investment unit, the issue price for such investment unit shall be determined in accordance with the rules stated in this paragraph. Such issue price attributable to each element of the investment unit shall be that portion thereof which the fair market value of such element bears to the total fair market value of all elements in the investment unit. The issue price of the bond or other evidence of indebtedness included in such investment unit shall be the portion so allocated to it. In the case of a bond or other evidence of indebtedness, or an investment unit as described in this paragraph (other than a bond or other evidence of indebtedness or an investment unit issued pursuant to a plan of reorganization within the meaning of section 368(a)(1) or an insolvency reorganization within the meaning of section 371, 373, or 374), which is issued for property and which—

(A) is part of an issue a portion of which is traded on an established securities market,

(B) is issued for stock or securities which are traded on an established securities market,

the issue price of such bond or other evidence of indebtedness or investment unit, as the case may be, shall be the fair market value of such property. Except in cases to which the preceding sentence applies, the issue price of a bond or other evidence of indebtedness (whether or not issued as a part of an investment unit) which is issued for property (other than money) shall be the stated redemption price at maturity.

(3) Issue date.—In the case of issues of bonds or other evidences of indebtedness registered with the Securities and Exchange Commission, the term “date of original issue” means the date on which the issue was first sold to the public at the issue price. In the case of privately placed issues of bonds or other evidences of indebtedness, the term “date of original issue” means the date on which each

such bond or other evidence of indebtedness was sold by the issuer.

(c) Bond with Unmatured Coupons Detached.—If a bond or other evidence of indebtedness issued at any time with interest coupons—

(1) is purchased after August 16, 1954, and before January 1, 1958, and the purchaser does not receive all the coupons which first become payable more than 12 months after the date of the purchase, or

(2) is purchased after December 31, 1957, and the purchaser does not receive all the coupons which first become payable after the date of the purchase,

then the gain on the sale or other disposition of such evidence of indebtedness by such purchaser (or by a person whose basis is determined by reference to the basis in the hands of such purchaser) shall be considered as gain from the sale or exchange of property which is not a capital asset to the extent that the fair market value (determined as of the time of the purchase) of the evidence of indebtedness with coupons attached exceeds the purchase price. If this subsection and subsection (a)(2)(A) apply with respect to gain realized on the sale or exchange of any evidence of indebtedness, then subsection (a)(2)(A) shall apply with respect to that part of the gain to which this subsection does not apply.